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CITATIONS

774381—48

In the Supreme Court of the United States

October Term, 1947

No. 516

The Ohio Oil Company, a Corporation, petitioner

v.

United States of America

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the circuit court of appeals (R. 387-401) is reported in 163 F. 2d 633.

JURISDICTION

The judgment of the circuit court of appeals was entered on September 10, 1947 (R. 401). On September 18, 1947, an order was entered extending through October 15, 1947 the time for filing a petition for rehearing (R. 401). The petition for rehearing, filed on October 15, 1947 (R. 422), was denied on October 22, 1947 (R. 423). The

petition for a writ of certiorari was filed on January 5, 1948. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether, where the United States and a lessee of public oil land enter into a contract agreeing that, for the purpose of computing the Government's royalties, the value of the royalty oil shall not be less than the reasonable minimum value determined by the Secretary of the Interior, the lessee is bound by the honest determination of the Secretary fixing the value, even though such amount is higher than that actually received by the lessee when it sold the oil.

STATEMENT

In August 1920, the oil and gas lease in controversy, covering 160 acres of public land in the Lance Creek oil field in Wyoming, was issued pursuant to the Mineral Leasing Act of February 25, 1920, c. 85, 41 Stat. 437 (30 U. S. C. 181, et seq.). Two years later, in 1922, the original lessee assigned the lease to The Ohio Oil Company (R. 301–315). The lease was for a term of 20 years, expiring August 25, 1940, with a preferential right of renewal for successive periods of 10 years "upon such reasonable terms and conditions as may be prescribed by the lessor, unless otherwise provided by law at the time of the expiration of such periods" (sec. 1, R. 302). Ohio was obligated to pay a

graduated percentage of the oil produced from the lease, but not less than 12½ percent (R. 303–304).

In each of the years 1930, 1935, and 1937, discoveries were made in progressively deeper sands, increasing the potential of the field from 165 barrels per day to 1,000 barrels per day in 1930, then to 3,000 barrels per day in 1935, and finally to 13,000 barrels per day in 1937 (R. 93–94). When the prolific deep sands were discovered in May 1937, Ohio's lease had only three years and three months more to run before it expired by its own terms. In the latter part of that year, Ohio and the owners of other leases in the Lance Creek field procured the approval of the Secretary of the Interior to a cooperative or unit plan agreement submitted by them for the development and operation of the field (R. 256–273).

The agreement incorporated by reference the applicable provisions of the Mineral Leasing Act, as amended (30 U. S. C. 226; 184). It extended the term of Ohio's lease which was nearing expiration, for so long as oil or gas was produced in paying quantities from any part of the land included in the unit plan (Par. XV, R. 268). Ohio agreed that royalty should be computed and paid in accordance with the rules and regulations approved by the Secretary, and in effect on December 1, 1936 (Par. I, R. 257; Par. X, R. 266). One of those regulations, Regulation 3 (e), provided that for the purpose of computing royalty, the

value of production should not be less than the reasonable minimum value determined by the Secretary.[1] In addition, Ohio consented to the conformation of the royalty requirements of the lease to the provisions of the agreement (Par. XIII (b), R. 267).

On May 31, 1939, more than a year after the effective date of the unit agreement, the Secretary of the Interior issued an order stating that, effective July 1, 1939, for the purpose of computing royalties due to the Government, the value of crude oil produced from federal land in the Lance Creek field was to be four cents per barrel above the price regularly posted by major purchasers of crude oil of 40° A. P. I. gravity in the Mid-Continent area (R. 226–227). At that time the posted price at Lance Creek was 77 cents per barrel, while the Mid-Continent price was $1.10 per barrel. Under the Secretary's determination royalties at Lance Creek would be computed on the basis of $1.14 per barrel, not 77 cents per barrel (R. 141–145).

Timely notice of the Secretary's action was sent to The Ohio Oil Company (R. 384–385), which requested a hearing with reference to the May 31, 1939 value order (R. 385–386). A hearing was held. The proceedings at the hearing were stenographically reported. Ohio introduced exhibits. After the hearing, but before decision,

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[1] For full text of Regulation 3 (e), see Appendix, p. 13.

Ohio was furnished with a memorandum, prepared in the Geological Survey, discussing the factors underlying the Secretary's determination. Ohio filed a response to the memorandum. After full consideration of all the evidence adduced, a decision was entered on February 13, 1941, and a formal order filed modifying the May 31, 1939, order so as to fix the value of Lance Creek oil for the purpose of computing royalties, at eight cents per barrel below the price regularly posted by the major purchasers for crude oil of 40° A. P. I. gravity in the Mid-Continent area (R. 293–295; 30 CFR, 1941 Supp., Part 222, 6 F. R. 1355). Expressed in figures the value of $1.14 per barrel fixed by the May 31, 1939 order was reduced to $1.02 per barrel by the modification of February 13, 1941. A motion for rehearing by Ohio was denied after full consideration expressed in a written opinion (R. 295–299).

This case is concerned with only the period from July 1, 1939, the effective date of the minimum value order, to April 1, 1941, when the Government commenced taking its royalty in oil. On October 28, 1941, the Department of the Interior made demand on Ohio for the payment of $9,186.96, representing the difference between royalties paid by Ohio computed on posted prices at Lance Creek field (77 cents per barrel) and royalties computed on the basis of the Secretary's minimum valuation order as modified ($1.02 per

barrel) (R. 327–328). When its demand was ignored, Interior threatened legal proceedings to cancel the lease unless the royalties were paid. Ohio then paid on condition that the money be held in a trust fund pending a judicial determination of the Secretary's authority to determine the minimum value of the oil for the purpose of computing royalties (R. 380–383). Interior agreed to this (R. 300–301).

Thereafter, suit was brought in the United States District Court for the District of Wyoming. The case presented three primary questions: (1) whether the district court had jurisdiction under the Tucker Act (28 U. S. C. 41 (20)); (2) whether the Secretary was authorized to fix the minimum value of the royalty oil; and (3) if the Secretary was authorized, whether the $1.02 value he fixed was arbitrary and unreasonable. The trial court sustained its jurisdiction, held that the Secretary was without power to fix the minimum value of the royalty oil, and concluded that the value fixed by the Secretary was "unlawful, inequitable, arbitrary and unreasonable" (R. 40–41). The same questions were presented on appeal to the circuit court of appeals (R. 388).

The circuit court of appeals sustained the jurisdiction of the district court under the Tucker Act, 28 U. S. C. 41 (20) (R. 388–392). However, on the merits, the circuit court of appeals held that Ohio and the United States had entered into a

contract (unitization and extension agreement) under which they had agreed that the value of production for the purpose of computing royalties was not to be less than the minimum value as determined by the Secretary; that the parties were free to contract on the subject and that the contractual power thus conferred on the Secretary was not in excess of his statutory power or unauthorized by law (R. 395–397). The circuit court of appeals pointed particularly to the Act of March 4, 1931, c. 506, 46 Stat. 1523–1525, amendatory of sections 17 and 27 of the Mineral Leasing Act (30 U. S. C. 226; 184), and to the Act of August 21, 1935, c. 599, sec. 1, 49 Stat. 674, 677, amendatory of section 17 of the Mineral Leasing Act (30 U. S. C. 226) as specifically authorizing the Secretary to require as a condition to his approval of the agreement extending the life of Ohio's lease and making it a part of the unit plan, that all development and operation under the unit plan be subject to the operating regulations in force when the agreement was made. It held that it was not improper for Ohio specifically to agree that the royalty to the United States on the oil produced under the lease as renewed should be computed and paid in accordance with the rules and regulations approved by the Secretary, and it further held as valid and subsisting, Regulation 3 (e), providing that for royalty-computing purposes the value of the oil was not to be less than

the reasonable minimum value determined by the Secretary (R. 397). The circuit court of appeals also held that the trial court erred in finding that the Secretary's $1.02 minimum value order was arbitrary inasmuch as the trial court had disregarded the factual basis upon which the Secretary had based his determination and had conducted a trial *de novo* on the question of value (R. 399-400). Accordingly, the circuit court of appeals reversed the judgment of the district court (R. 401).

ARGUMENT

1. The lease (R. 301–311) and unit plan agreement (R. 256–284) together constitute the contract between The Ohio Oil Company and the United States. The unit plan agreement recites that royalties "shall be computed and paid in accordance with rules and regulations approved by the Secretary * * *" (R. 266) and that "all development and operation under this agreement shall be subject to the operating regulations * * * in effect on December 1, 1936 * * *" (Par. I, R. 257). Regulation 3 (e), one of the operating regulations the contract thus made applicable (see Appendix, p. 13), provides that for the purpose of computing royalties the value of production shall not be less than the reasonable minimum value determined by the Secretary. In addition, Ohio specifically consented to the alteration of the "royalty require-

ments" of its lease and "the regulations in respect thereto to conform said requirements to the provisions of this agreement" (Par. XIII (b), R. 267). Thus, by contract the parties agreed that for royalty-computing purposes, the value of production was not to be less than the reasonable minimum value determined by the Secretary.

2. There is clear statutory authority for the Secretary so to contract. The Act of March 4, 1931, c. 506, 46 Stat. 1523–1525, amending sections 17 and 27 of the Mineral Leasing Act (30 U. S. C. 184, 226),[2] authorizes Government lessees in an oil or gas field to join in a unit plan for the development or operation of the field where the Secretary of the Interior approves. It provides that any lease becoming the subject of such a plan was to continue in force "until the termination of such plan." In unequivocal language, the 1931 Act empowers the Secretary, in his discretion, with the consent of the lessees "to establish, alter, change, or revoke" "royalty requirements of such leases" and to make such regulations with reference to the leases with the consent of the lessees "as he may deem necessary or proper to secure the proper protection of such public interest."

[2] The circuit court of appeals placed primary reliance on the specific provisions of this statute as the source of the Secretary's power to contract as he did with Ohio (R. 395–397). Yet the petition makes no mention of this statute either in the text or in the appendix.

As previously stated (supra, pp. 8–9), the Secretary, with Ohio's consent, did alter the royalty requirements of the lease by making the 1936 regulations with respect to the computation of royalties a part of the unit agreement. This contract, whereby the parties agreed the Secretary might determine the reasonable minimum value of royalty oil, easily falls within the authority of the statute.

3. Petitioners assign as error the failure of the circuit court of appeals to hold that the Secretary's finding of $1.02 value was arbitrary and unreasonable (Pet. 8).[3] There is no claim or finding in the case that the Secretary's determination of $1.02 per barrel is fraudulent or dishonest. From that standpoint, therefore, the determination is binding on Ohio. *Goltra* v. *Weeks,* 271 U. S. 536, 547, 548; *Kihlberg* v. *United States,* 97 U. S. 398, 401, 402; *Gillioz* v. *Webb,* 99 F. 2d 585, 587 (C. C. A. 5).

If Ohio wished to attack the Secretary's value determination as unreasonable, it was obligated first to show the basis of the Secretary's action. This it did not do. It failed to put into the record the evidence on which the Secretary's finding, as shown by its recitations, is based (R. 293–295). Accordingly, on the record in this case the peti-

[3] Petitioner offers no reasons or argument in support of this or the other specifications of error it lists in its petition (Pet. 8).

tioner is in no position to demonstrate, even if it could, that the order was not founded on reason. Cf. *Miss. Valley Barge Co.* v. *United States,* 292 U. S. 282, 286; *Edward Hines Trustees* v. *United States,* 263 U. S. 143, 148.

What the trial court did was to proceed *de novo* on the identical question of value determined by the Secretary. In this the trial court erred. As pointed out by the circuit court of appeals (R. 400): "We do not think the trial court was at liberty to disregard or ignore the factual basis upon which the Secretary proceeded, nor was it at liberty to substitute its concept of value for that of the Secretary. We should remember that the contract authorized the Secretary, not the court, to determine the reasonable minimum value of the royalty oil."

Ohio insisted the 77-cent price posted at Lance Creek field was controlling, but the circuit court of appeals could find no justification for the 25-cent differential since the record before it showed that "oil of inferior grade and quality, produced in the same country, and transported to the same markets under similar conditions as the Lance Creek oil, sold at $1.02 [the value fixed by the Secretary] per barrel" (R. 400).

CONCLUSION

The questions presented by the petitioner were correctly decided by the circuit court of appeals, and no conflict of decisions is present. The peti-

tion for a writ of certiorari, therefore, should be denied.

Respectfully submitted.

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JANUARY 1948.

APPENDIX

Excerpts from Department of the Interior, *Oil and Gas Operating Regulations Applicable to Lands of the United States, Etc.,* Revised November 1, 1936.

SECTION 3—MEASUREMENT OF PRODUCTION AND COMPUTATION OF ROYALTIES

* * * * *

(e) *Price basis for computing royalties.* The value of production, for the purpose of computing royalty, in the discretion of the Secretary of the department having jurisdiction over the leasehold, may be calculated on the basis of the highest price per barrel, thousand cubic feet, or gallon, paid or offered (whether such price is established on the bases prescribed in these regulations or otherwise) at the time of production in a fair and open market for the major portion of like-quality oil, gas, natural or casing-head gasoline, propane, butane, and all other hydrocarbon substances produced and sold from the field where the leased lands are situated; but under no conditions shall the value of any of said substances for the purpose of computing royalty be deemed to be less than the gross proceeds accruing to the lessee from the sale thereof or less than such reasonable minimum price as shall be determined by said Secretary.

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